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MATTERS RELATING TO THE PROGRAMME CYCLES

Request from the Government of Albania for "as if" LDC Status

Report of the Administrator

I. PURPOSE

1. The present report provides the additional information requested in Governing Council decision 93/23 and supplements the information provided by the Government of Albania (see annex). It is intended to assist the Executive Board in its consideration of "as if" least developed countries (LDC) status for Albania.

II. JUSTIFICATION

2. The Government of Albania justifies its request for "as if" LDC status on the basis of the four formal criteria established by the Committee on Development: population, income, quality of life and potential for economic diversification. The application of these criteria in the case of Albania is outlined in the annex to the present document. Some members of the Governing Council had an opportunity to see at first hand the conditions in Albania in August 1993, when a group from the Standing Committee for Programme Matters visited the country as part of the 1993 review of UNDP operations in the Europe and Commonwealth of Independent States region.

3. To avoid a mechanistic or rigid interpretation of the four formal criteria, the Committee on Development Planning has established that complementary criteria can be taken into account and that they should be applied flexibly. This recommendation allows for the consideration of additional special indicators in determining a country's claim to "as if" LDC status that more accurately reflect the structural and dynamic characteristics of the existing situation in a country. In this regard, it is important to note that Albania is

at present having to face greater human hardship and fragility than is reflected in the numbers provided in the annex. For example:

(a) In the agricultural sector, where most of the population live and make their living, most of the holdings - often scattered among two or three plots - have proven to be too small to produce enough to feed a family. In addition, the commercial agricultural sector has suffered from wide fluctuations in production and quality from year to year because of the low level of technology and the concomitant sensitivity of productive capabilities to abnormal climatic occurrences;

(b) The country's energy supply is heavily dependent on hydroelectric power, which is very variable, especially as a result of frequent breakdowns and down time. This lack of reliability makes it difficult to fulfil contracts for the export of electric power to neighbouring countries;

(c) Virtually all of the country's infrastructure is in a deplorable state of neglect and therefore requires costly repairs or replacement;

(d) The export of minerals has in the past provided the country with 20 per cent of its foreign exchange earnings; however, owing to price volatility and the difficulties of finding the capital to maintain productivity, this sector cannot be relied on to sustain the inflow of foreign exchange;

(e) There is a need for a significant quantitative and qualitative increase in education and training programmes to upgrade the skills of those of working age and those in schools and universities, especially with regard to the application of the available current information technologies, without which the rate of increase in the productivity of Albanian workers can be expected to remain low.

4. From the information provided in the annex, it is clear that Albania meets two of the four criteria for LDC status (population and income). In addition, the weight of the supplementary criteria should constitute an important factor in considering a justification for granting Albania "as if" LDC status. The Government of Albania has requested that the eligibility criteria for this classification be interpreted in a manner that gives due weight to the exceptional factors of Albania's current and immediate future circumstances of severe poverty and the extreme difficulties and dangers of the transition from a centrally planned to a market economy, and from an authoritarian regime to a democratic society.

5. The expectation of the Government is that the Albanian people will be able to benefit - on a temporary and exceptional basis - from this special programme of aid directly to those countries classified as LDCs. They believe that the General Assembly, in adopting resolution 2564 of 13 December 1969, created the LDC category in order to permit low-income countries with special problems to benefit from exceptional measures. A great deal is at stake in assuring the successful navigation of the difficult and dangerous passage to the status of a normal developing country. It is with this in mind that the Government has decided to apply for "as if" LDC status.

III. EXECUTIVE BOAPD ACTION

6. Should the Executive Board agree to the request from the Government of Albania, it may also wish to authorize the Administrator to allocate an additional $1.6 million to the fifth cycle indicative planning figure (IPF) resources for Albania.

Annex

REQUEST FROM THE GOVERNMENT OF ALBANIA FOR "AS IF" LDC STATUS

I. INTRODUCTION

1. Albania is a small country in the Balkan region with a population of 3.3 million, two thirds of whom live in rural areas and with half engaged directly in the agricultural sector. It is also the poorest country in Europe with a 1992 per capita income most recently calculated by the World Bank at $290, with a similar figure projected for 1993 (according to the World Bank Atlas methodology, as illustrated in the World Bank President's Report for a Technical Assistance Project which includes a Country Assistance Strategy (WB P6058/Alb, August, 1993). Albania is in the early phase of its emergence from a 45-year period under a despotic, autarkic, command economy system that left it with a stagnant economy and a population caught in a trap of low productivity. Indications of its break from international isolation were signalled in 1991, when Albania became a member of the World Bank and the International Monetary Fund (IMF) and of the European Conference on Security and Cooperation. After the 1992 election, the new democratic Government initiated an ambitious programme to build a new market economy, with massive foreign assistance, including the international financial institutions, the G-24 and the European Community. It must be stressed that because of Albania's very weak external position in the wake of the collapse of the centrally planned, autarkic system, the country will need access to concessional aid over the foreseeable future in order to turn around the economy. While such assistance has been available initially, it is now a major challenge to the international community to provide assistance, beyond food and humanitarian aid, in support of programmes that have been designed to deepen structural reforms, provide infrastructure and strengthen the social safety net.

The difficult transition to a market economy and a democratic society

2. The rapid and complete collapse of the previous system in the last years of the 1980s was characterized by a demoralizing and debilitating paralysis of the political, economic, financial, administrative and social structures of the country. Until wide-ranging systemic changes could be achieved to set the economy on a sufficiently productive path, there was an immediate need for massive food aid from the international community in order to avoid famine, epidemics and rioting. Widespread malnutrition still prevails and over half of the labour force is still unable to find productive employment. Among the youth, unemployment is estimated as high as 60 per cent. The combination of these factors has contributed to a situation that is fragile and volatile with a great potential for mass violence and civil disobedience. It is expected that it will take several years before the Albanian economy is growing rapidly and equitably enough to ensure social and political stability.

3. The election of March 1992 brought a democratic government to power that quickly embarked on a negotiated stabilization and restructuring programme that has been underpinned by an IMF Stand-by Arrangement. This has involved constitutional change and the adoption of new laws on commerce, industry,

employment, private property, investment, agricultural land reform and taxes. However, the implementation phase has been proving extremely difficult owing to the shortage of qualified personnel, the lack of financial resources and the stresses associated with the process of restructuring. Despite this, the IMF Stand-by Arrangement has produced remarkably good results; for example, monthly inflation came down from 10-15 per cent in 1992 to less than 2 per cent on average in 1993; reserves rose from zero to manageable levels; and the exchange rate has been stable for the past 12 months. All of the targets of the IMF Stand-by Arrangement have so far been met. None the less, Albania's future stability still depends on further painful economic measures, such as cut-backs in subsidies and the curtailment of social expenditure programmes to make them more cost-effective so that fiscal consolidation can be achieved. These tasks, however, could not be carried out without the continued support of the international community.

4. The economic, social and financial situation has recently suffered an additional setback from the adverse impact on Albania of the Security Council's sanctions against Serbia and Montenegro and the increased regional tension and instability in Kosovo and the former Yugoslav Republic of Macedonia. This has resulted in strained relations with Greece, further exacerbating the stress. The most direct impact has been the return from Greece of more than 20,000 Albanians that have to be fed, housed and integrated into an economy stretched to the breaking point.

5. In the urban areas there are further causes of political discontent and unrest arising from:

(a) Expectations of improvements in the inadequate system of water and electricity supply that have not materialized;

(b) Growing unemployment amounting to over 300,000 jobless persons resulting from the slowness of the recovery of industrial activity. Less than 20 per cent of the country's industrial productive capacity is operational because of the very limited domestic pool of capital and entrepreneurs and the lack of foreign investment that, in turn, is in large part attributable to an increasingly unstable economic and political situation. Foreign investment has also been affected by the very bad state of repair of infrastructure and its absence, so that basic services (electricity, telephone, fax, cable, water and sewage) are lacking or inadequate - again, areas where external assistance will be essential to create new conditions;

(c) Absence of effective programmes to alleviate poverty that is reaching crisis proportions (benefits from the Social Protection Scheme have dropped from an average of $18 per month to $5 per month) and the low expec ations that such programmes will be developed and implemented;

(d) Poor housing conditions, lack of funding for repairs, and new construction;

(e) Services in such essential areas as health and education have been affected by cut-backs in the budget that were necessary because of the poor

fiscal condition in the country - to redress the situation, Albania needs not only resources but also external assistance in order to modernize these programmes and make them more cost-effective.

II. JUSTIFICATION

6. The situation in which the Albanian people find themselves can have a positive denouement if, in addition to the sacrifices and discipline of the Albanian people themselves, the international community continues to provide the necessary financial assistance and technical cooperation. The support provided by the specialized agencies of the United Nations system has proven indispensable in initiating the design and implementation of the programme of economic reform. However, in face of the magnitude and complexity of the task on which Albania has embarked, the assistance from both bilateral and multilateral sources needs to be adjusted to include more technical cooperation of a capacity-building nature (in addition to food and other forms of humanitarian aid) so as to increase Albania's absorptive capacity for all forms of aid. At present, the total volume of development assistance is much below levels required. The IPF amounts to only $6 million over the five-year period from 1992 to 1996, of which only 75 per cent has been released for programming. This would be supplemented by the special United Nations programmes that would become available under the "as if" LDC status, which provide both technical cooperation and capital assistance to the poorest countries and which would assist the Albanian people, who are grappling with an exceedingly difficult and dangerous developmental and transitional challenge.

7. The Committee on Development Planning recommends four formal criteria of eligibility for LDC status: population, income, quality of life and potential for economic diversification. With regard to these formal criteria, the situation of Albania is described below:

(a) Population. The criterion is that a country must have a population under 75 million. Albania meets this criterion;

(b) Income. The criterion is that the country's average per capita income be less than $600 for the period 1986-1988. The gross national product (GNP) figures for Albania during those years are unreliable and not comparable to those based on current United Nations methodology for computing national accounts. Thus, figures for the average per capita income prior to 1990 are not considered accurate although they were used to calculate the 1992-1996 IPF. They were used because the standard procedure for calculating IPFs does not allow for exceptions. Currently, Albania's average per capita income according to the World Bank is $250 (see para. 1);

(c) Quality of life. The criterion requires a value of 47 or less on the augmented physical quality of life index (APQLI), which is composed of four variables: (a) expectation of life at birth; (b) level of literacy; (c) rate of school attendance, for both primary and secondary levels; and (d) the average caloric intake per person per year. A closer look at these elements of the situation reveals the following:

(i) Life expectancy. On the basis of data from the 1989 census, the expectation of life at birth was 72.2 years in 1990, 69.3 years for men and 75.4 years for women. However, Albania is struggling to preserve these life expectancy levels as it copes with the decline in incomes and with a decline in nutrition. The health situation has also deteriorated: almost all primary care facilities and hospitals have ceased to function properly as a result of the lack of preventative maintenance, basic equipment is missing and drug production and distribution are at a near standstill. At the same time, the network of hospitals far exceeds Albania's maintenance capacity and ability to provide efficient service;

(ii) Literacy and (iii) School attendance. Albania boasted a 99 per cent enrolment of the relevant age group in the primary school system during the period 1986-1990. This percentage drops off dramatically at the secondary level to about 64 per cent. Less than 8 per cent of the population over the age of 10 were classified as illiterate in 1989. However, these figures are considered deceptive given the tendency of the previous regime to exaggerate achievements. In any case, it is estimated that since 1991 there has been a sharp decline of well over 10 per cent in educational attendance at all levels. Damaged school buildings and the obsolete curricula are also contributing factors; given the extremely tight fiscal situation over the medium term, they can be tackled only with substantive external assistance, providing both capital for rehabilitation of physical installations and technical cooperation for improved management, new curricula and new textbooks. This is particularly true for education in rural areas, where standards are reported to have been deteriorating over a longer period of time and where many parents prefer to have their children tend to agricultural and domestic chores. When new literacy levels are determined, they will undoubtedly reflect this deterioration in the educational system;

(iv) Nutrition. Prior to 1990, government statistical records show Albania's average daily consumption per capita to be above 3,000 calories. A calorie study carried out by the Food and Agriculture Organization of the United Nations (FAO) in 1991 showed consumption closer to 2,600 calories per person. This latter level of daily per capita intake (likely to be more accurate) is only slightly above that of the average in LDCs and lower than the average of the developing countries (see the United Nations Children's Fund (UNICEF) report entitled, The State of the World's Children, 1993, p. 71);

(d) Diversification. The Economic Diversification Index (EDI) is comprised of four variables: (a) the proportion of the population engaged in industry; (b) the proportion of manufacturing in GDP; (c) per capita consumption of electricity; and (d) the level of exports. Because of autarkic policies, Albania developed its industrial sector beyond that characteristic of a typical developing country, with industry accounting in 1990 for about 40 per cent of the country's total output and employing over 20 per cent of the nation's work force, according to statistics available at the time. Since then, the contribution of manufacturing in terms of both output and employment has fallen

sharply. Industry's share in GDP came down to around 10 per cent by the end of 1993, reflecting the collapse of the inefficient, centrally planned, State-owned enterprise sector in 1991-1993. Some further points should also be noted: (a) at the peak of industry's share, in GDP, some 200,000 of the 33 per cent unemployed in the country were in industry/mining; (b) massive industrial restructuring, downsizing and privatization is imperative to scale back inefficient production, reduce the lingering fiscal burden of budget support to inviable enterprises, and to encourage efficient production in areas where the country's comparative advantage offers new, competitive opportunities. The preliminary estimate of the EDI index for Albania is 37.7. This is above the maximum of 22 set by the Committee on Development Planning; however, given the conceptual difficulties and formidable task of making this estimate for the years involved, not much reliance can be placed on this estimate either as an order of magnitude or as precisely as a decimal point would suggest. This figure, however, has dropped significantly since 1990, that is, after the collapse of the previous system and the subsequent introduction of the reform programme.